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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 516.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Petitioner*,

v.

O. G. RICHTER, *Respondent*.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

BRIEF FOR THE RESPONDENT.

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BRIEF FOR THE RESPONDENT.

OPINIONS BELOW.

The memorandum opinion of the United States Board of Tax Appeals (R. 16-17) is not officially reported. The opinion below of the United States Circuit Court of Appeals for the Third Circuit (R. 28-30), affirming the decision of the United States Board of Tax Appeals, is reported in 114 F. (2d) 452.

QUESTION PRESENTED.

This case was tried before the United States Board of Tax Appeals (hereinafter sometimes referred to as the Board) on the issue of tax liability under Section 166 of the Revenue Act of 1934.[1] From a decision in favor of the Respondent, the Commissioner appealed to the United States Circuit Court of Appeals for the Third Circuit (hereinafter sometimes referred to as the Circuit Court of Appeals) and thereafter asserted that the Respondent was liable for taxes under Section 22(a) of the Revenue Act of 1934.[2] The Court held that the Board had committed no error and that the Court could not review an issue which had never been presented to the Board (R. 28-30).

The writ of certiorari granted by this Court (R. 31) limits review of this case to the question "whether, by

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[1] Sec. 166. Revocable Trusts.

Where at any time the power to revest in the grantor title to any part of the corpus of the trust is vested—

(1) in the grantor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom, or
(2) in any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom,

then the income of such part of the trust shall be included in computing the net income of the grantor. [U. S. C. Supp. V, Title 26, Sec. 166.]

[2] Sec. 22. Gross Income.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, . . . of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * [U. S. C. Supp. V, Title 26, Sec. 22.]

invoking the general gross income provisions of Section 22, the Commissioner had so changed the theory of the Government's case on appeal as to preclude the Circuit Court of Appeals from considering the issue". (Petition for Writ of Certiorari herein, page 2.)

In the light of the Commissioner's brief, this question involves the further questions of whether the Respondent was advised with fair certainty before the Board that the Commissioner was asserting a claim against him of tax liability based upon the provisions contained in Section 22(a) and whether the appellate court should have considered the new issue of law and fact which was not raised in the trial tribunal.

STATUTES AND REGULATIONS INVOLVED.

Section 22(a) and Section 166 of the Revenue Act of 1934 have been set out in footnotes. Article 166-1 of Regulations 86, as amended by Treasury Decision 4629 (1936), appears in Appendix E to the Commissioner's Brief, pp. 63-65.

STATEMENT.

In December, 1930, the Respondent created a trust under which the net income was payable to the Respondent's wife. He designated as sole trustee The Union Trust Company of Pittsburgh, which held all entrusted securities in its own name. Under the trust instrument, the trustee alone had power to hold and invest the trust securities; to convert and sell them; to reinvest the proceeds as it should deem safe; to collect interest, income, dividends and profits; to pay the expenses of management, and to pay over the balance of such income to the beneficiary in such installments as she might request.

The trust was revocable only on notice by the Respondent together with the written consent of the beneficiary. The Respondent did not at any time have any agreement with his wife, nor had he ever asked his wife, to consent to a termination of the trust. By its terms the trust was to expire in January, 1936, but in 1932 the term was extended to January, 1938. Otherwise, the trust was to terminate upon the earlier death of the settlor or of the beneficiary.

The entire net income was paid by the trustee to the beneficiary from the date of the creation of the trust in 1930 to the termination thereof in November, 1935, when the beneficiary died. The beneficiary reported the income received from the trust in 1934 in her income tax return for that year (the only year here involved). On the basis of Section 166 of the Revenue Act of 1934, the Commissioner of Internal Revenue added the net income from the trust to the Respondent's reported net income and determined a deficiency in his tax for 1934. In a statement accompanying the notice of deficiency, the Commissioner explained the changes as follows:

> "The record indicates that under the provisions of section 166 of the Revenue Act of 1934, the trust created by you in 1930 for the benefit of your wife, Nannie C. Richter, was a revocable trust and, therefore, the income is taxable to the grantor" (R. 7).

The Respondent appealed to the Board, contending that he, as grantor, did not retain under the trust instrument power to revest the trust corpus within the meaning of Section 166. Before the Board, the Commissioner contended that the trust income was taxable to the grantor under Section 166 of the Revenue Act of 1934 and made reference to Article 166-1 of Regula-

tions 86, as amended, which, he said, "fairly represent the intended application of the provisions of Section 166 of the Revenue Act of 1934." The Board noted as follows:

> "The [Commissioner], in adding the trust income to [the grantor's] income for 1934, has proceeded on the theory that section 166 of the Revenue Act of 1934 makes the trust income taxable to the grantor of the trust" (R. 17).

In determining the sole issue before it, the Board held that the trust income was not taxable to the grantor for the year 1934.

The Commissioner sought review of the Board's decision by the Circuit Court of Appeals, assigning as error the failure of the Board to hold that the trust income was taxable to Respondent under Section 166 and Article 166-1 of Regulations 86, as amended in 1936 (R. 20). On motion of the Commissioner, agreed to by the Respondent herein, preparation of the record for review was held in abeyance pending the decision of this Court in the case of *Helvering* v. *Wood,* 309 U. S. 344, for the reason that "the issue involved in this case is similar to that presented in the [*Wood*] case". Following that decision, the Commissioner filed in the Circuit Court of Appeals a Statement of Points to be Relied Upon (R. 22-23) in which he alleged that the Board also erred in failing to hold the trust income taxable to the Respondent under Section 22(a) of the Revenue Act of 1934. This was clearly an afterthought and an attempt to bring in a new issue which had not been preserved by his assignments of error filed long before. Thereupon the Respondent objected to the inclusion in the record of this Statement of Points to be Relied Upon (R. 25). When the Commissioner, in his brief

before the Circuit Court of Appeals, subsequently abandoned Section 166 as a ground for the reversal of the Board's decision, the Respondent moved to strike the Statement of Points to be Relied Upon and moved to dismiss the appeal (R. 26-27). Although the Respondent thus opposed the manner in which the Commissioner sought to raise on appeal a new issue which had not been tried below, the Circuit Court of Appeals preferred to affirm the Board's decision on the ground, as Respondent also contended, that the Board had committed no error and that an appellate court could not consider an issue which had never been presented to the Board (R. 28-30).

SUMMARY OF ARGUMENT.

We shall contend:

(1) Contrary to what the Commissioner has endeavored to show from sources within and without the record, it is clear beyond any question that there is nothing in any of the proceedings in this case which affords any basis for the right of the Commissioner to assert on appeal the applicability of Section 22(a). This issue was not raised directly or indirectly before the Board or, to begin with, before the Circuit Court of Appeals. Any attempt on the part of the Commissioner to claim that such issue was present before the Board by virtue of reference in the proceedings there to Article 166-1, as amended, is not borne out by the facts, and furthermore, all reference to such Article for any purpose was abandoned before the Circuit Court of Appeals.

(2) Article 166-1, as amended in 1936, could not be the basis for the assertion of tax liability under Section 22(a). Any other result would be contrary to other portions of the same Regulations 86 which advises tax-

payers that each article is to be read as an interpretation of the corresponding section of the Act. Then, too, the Article amended in 1936 could not have any bearing on a tax liability asserted for the year 1934. *Helvering* v. *Wood*, 309 U. S. 344; *Helvering* v. *Clifford*, 309 U. S. 331. If such Article goes to the extent the Commissioner claims, it is invalid.

(3) The Circuit Court of Appeals, in refusing to consider the new issue first raised in that Court, followed the well defined law on the subject. *Helvering* v. *Wood*, 309 U. S. 344; *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200.

POINT I.

None of the Proceedings in this Case Affords Any Basis for the Right of the Commissioner to Assert on Appeal the Applicability of Section 22(a).

Because of the many curious turns and twists which the Commissioner has given to this case since it began with the issuance of the ninety day letter (R. 4-7), he apparently found it necessary to have recourse, in an effort to find some basis for his contentions before this Court, to the briefs and various other documents outside of the record. Notwithstanding that, the proceedings in this case, whether within or without the record, disclose that the very first time that the Commissioner advanced a "substantial incidents of ownership" argument within the meaning of Section 22(a), or pursuant to what this Court said in *Helvering* v. *Clifford*, 309 U. S. 331, was after his appeal had been taken to the Circuit Court of Appeals. Likewise, it is equally clear that the first time that the Commissioner relied upon Article 166-1, as amended, of Regulations 86 as an independent basis for raising an issue under Section

22(a) was in his petition to this Court for writ of certiorari. To outline these various steps in the pending litigation, the Respondent also must now refer to documents outside of the record.

At the outset of the present tax dispute, the Commissioner in a ninety day letter asserted a tax deficiency on the basis of Section 166, as follows:

> "The record indicates that under the provisions of section 166 of the Revenue Act of 1934 the trust created by you in 1930 for the benefit of your wife, Nannie C. Richter, was a revocable trust and, therefore, the net income is taxable to the grantor. In accordance with the provisions of the trust instrument, the trust could be terminated by you at any time with consent of the beneficiary and the title to the corpus would revest in the grantor upon the exercise of such power" (R. 7).

In that letter he also advised the Respondent that he might "file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency" (R. 5). The Respondent then appealed to the Board, contending that the trust was not revocable as alleged by the Commissioner in his deficiency letter (R. 3-4). In answer thereto the Commissioner denied this contention, but did not by an affirmative defense plead or otherwise assert the applicability of Section 22(a). The parties proceeded to frame a stipulation (R. 8-10) with regard to the only issue raised[1]—that the income was taxable under Section 166. In the preparation of the evidence and in his brief before the Board, Respondent directed himself solely to the proposition that his reversionary interest under the trust instrument

[1] There was one other issue which was disposed of by Paragraph X of the Stipulation (R. 10) and which is of no importance here.

did not give him "a power to revest . . . title to any part of the corpus of the trust" within the meaning of Section 166, and that if Section 166 of the Revenue Act of 1934 was so construed, it was invalid (Appendix, p. 30). The Commissioner's nineteen page brief before the Board argued that the trust income was taxable to Respondent under Section 166. The Commissioner there stated the "Question Presented", as follows:

> "Is the income realized by the trust created by the petitioner on December 29, 1930 taxable to the petitioner as grantor under the provisions of section 166 of the Revenue Act of 1934?" (Appendix, p. 31).

In a one page argument, the Commissioner also contended that Respondent was taxable under the provisions of Article 166-1, as amended, on the ground that the revesting provisions of the trust constituted a failure to part with the substantial incidents of ownership. (See Appendix A to Brief for Commissioner herein.) Obviously this point was advanced in support of tax liability under Section 166, for the Commissioner argued:

> "[Commissioner] contends that the regulations are reasonable and *fairly represent the intended application of the provisions of Section 166 of the Revenue Act of 1934* and that the application of the regulations to the facts of the instant case clearly requires that the Commissioner's determination of deficiency for the year 1934 should be sustained." (Appendix A to Commissioner's Brief.) (Italics supplied.)

The Commissioner's brief before the Board did not mention the now asserted applicability of Section

22(a); it concluded with the statement that "It follows that the determination of the Commissioner of Internal Revenue should be approved." This determination, as shown above, was that the income was taxable to the taxpayer under Section 166.

Clearly the Commissioner was relying at all times before the Board upon Section 166. Certainly the Respondent took that position in his reply brief before the Board. In that brief the Respondent concerned himself with distinguishing under Section 166 a revocable trust and one which revested[1], and, consequently, was only incidentally concerned with Article 166-1, as amended, contending that it was invalid to the extent that it went beyond the statutory provisions of Section 166. (See Appendix B to Brief for Commissioner herein, pp. 57, 58.) Certainly, too, the Board likewise understood that the sole issue raised was with regard to Section 166 of the Revenue Act of 1934. In its opinion the Board said:

> "The respondent, in adding the trust income to petitioner's income for 1934, has proceeded on the theory that section 166 of the Revenue Act of 1934 makes the trust income taxable to the grantor of the trust" (R. 17).

At another place the Board said:

> "The issue left for decision is whether the trust income is taxable to the petitioner under Section 166 of the Revenue Act of 1934" (R. 16).[2]

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[1] This distinction was pointed out by this Court in *Helvering* v. *Wood*, 309 U. S. 344, 347.

[2] See footnote p. 8.

From the foregoing it is obvious that the Commissioner, despite his present assertions, did not contend before the Board that the Respondent was taxable either under the authority of Section 22(a) of the Revenue Act of 1934 or under Article 166-1, as amended, in so far as that Article can be said to authorize taxation under Section 22(a), nor did he advance a similar argument.

Upon consideration of the only issue before it, the Board held that the trust income was not taxable to the Respondent for the year 1934 (R. 17). Thereupon the Commissioner filed a petition for review in the Circuit Court of Appeals in which he assigned as error the failure of the Board to hold that such income was taxable under Section 166 and Article 166-1 of Regulations 86, as amended. Section 22(a) was not mentioned; nor was Article 166-1, as amended, made the separate basis of an assignment of error; nor was error assigned for failure of the Board to hold that Respondent was in substance the owner (R. 20). That the Commissioner, after taking this appeal, still considered that the sole issue was based on Section 166, is manifested by his motion to withhold preparation of the record until this Court should decide the then pending case of *Helvering* v. *Wood*. In this motion, agreed to by the Respondent, he stated:

> "The issue involved in this case is similar to that presented in the case of *Commissioner* v. *Meredith Wood*, B. T. A. Docket No. 88426, (37 B. T. A. 1065)" (Appendix, p. 32).

It will be recalled that the *Wood* case had been litigated in the Board of Tax Appeals and in the Circuit Court of Appeals on the basis of Section 166 see *Helvering* v. *Wood*, 309 U. S. 344.

After the decisions by this Court in the *Wood* and *Clifford* cases, the Commissioner filed a so-called "Statement of Points to be Relied Upon" in the Circuit Court of Appeals (R. 22, 23). This was merely an afterthought. It was a mere attempt by a new procedural form that had just been adopted by the Circuit Court of Appeals to change the *Wood* case issue of Section 166 (upon which the appeal in the instant case was being stayed, as above pointed out) to a *Clifford* case issue of Section 22(a). This pleading was not a proper one either from the procedural standpoint or under the Rules of the Circuit Court of Appeals, and by it the Commissioner had no right to undertake to raise the new issue of Section 22(a). (See Objection (R. 25), and Motions (R. 26, 27).) In that Statement of Points not only will it be noted that the Commissioner sought to raise Section 22(a) for the first time, but it will also be noted that he did not rely upon Article 166-1 of Regulations 86, as amended, either as a basis for raising Section 22(a) or as a separate basis for asserting tax liability.

This same observation should also be made of the Commissioner's brief in the Circuit Court of Appeals. Therein, the Commissioner abandoned all reliance upon Section 166. In this connection he said at page 7 of his brief in the Circuit Court of Appeals:

> "In view of the decision in the *Wood* case, we are not here contending that Section 166 is applicable to the instant case. But we do believe and submit that Section 22 may properly be considered on this appeal and that under the *Clifford* case the Commissioner is entitled to a reversal here."

The Commissioner did not rely upon Article 166-1, as amended, in raising the issue of Section 22(a), nor

even urge its applicability. The Commissioner at page 7 of his brief said:

> "To be sure, Section 22 is not specifically mentioned in the assignments of error. We believe, however, that errors numbered 2, 4, 5 and 6 are clearly broad enough to cover the question."

Errors 2, 4, 5 and 6 were merely general in nature and made no reference to Article 166-1, as amended (R. 20), whereas that Article is specifically referred to, along with Section 166, in errors numbered 1 and 3 (R. 20). The Commissioner thus avoided urging errors numbered 1 and 3 "to cover the question" of the applicability of Section 22(a), although he is now relying upon those avoided errors for support of his argument before this Court. While the abandonment of reliance on Section 166 would seem of necessity to work an abandonment of Article 166-1, as amended, which depended for life upon Section 166,[1] it is apparent in any event that reliance upon Article 166-1, as amended, either alone or as a stepping stone to Section 22(a) was abandoned as fully as if the Commissioner had said so in so many words.

Furthermore, it is interesting to note in this connection that not only was Article 166-1 of Regulations 86, as amended, not even mentioned once in the body of his brief before the Circuit Court of Appeals, but also that in the Appendix thereto the Commissioner merely printed Article 166-1 of Regulations 86 as that Article existed before it was amended by Treasury Decision in 1936. How then can the Commissioner now be heard to urge legitimately that he has at all times

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[1] See pages 17-18 *infra* where the pertinent portions of Regulations 86 are quoted. They fully support this statement.

before the Board and also before the Circuit Court of Appeals, relied upon Article 166-1, as amended, as a basis for taxing the Respondent under Section 22(a)? It has been conclusively shown above that in the Circuit Court of Appeals the Commissioner did not rely upon Article 166-1 of Regulations 86, as amended, in any manner whatsoever. And in the Board, this Article was barely mentioned in the Commissioner's brief, and nowhere else, and then only in support of his argument based on Section 166.

As to the Commissioner's attempt to raise Section 22(a) for the first time in the Circuit Court of Appeals, the Respondent objected to the unwarranted use of a Statement of Points in an effort to raise the issue (R. 25). Respondent also objected by motion (R. 26, 27) and by brief to the Commissioner's raising of the Section 22(a) issue on the ground that it had not been tried before the Board and on the ground that such an issue had been in effect waived by prior proceedings. While these procedural arguments were before the Court, the Circuit Court of Appeals chose to rest its opinion upon established principles of jurisdiction governing appeals. Under those principles, often approved by this Court, the appellate court could not determine a new issue which had never been prepared for trial, and, accordingly, it could not consider the applicability of Section 22(a). Before the Circuit Court of Appeals the Commissioner did not attempt to show that the issue raised by the interjection of Section 22(a) was not a new issue. Rather, at page 8 of his brief, he admitted:

> "While it may be that the Board was not asked to pass upon the applicability of Section 22(a) in the instant case, and did not purport to do so, still it seems plain that the taxpayer may not avoid just

taxes because the Commissioner may have given an erroneous reason for the assessment."

Since the Circuit Court of Appeals had never been requested to find the Respondent taxable on the basis of Article 166-1, as amended, either alone or in conjunction with Section 22(a), it naturally could not consider that question, nor could it be held to have committed reversible error for failing to consider the question which was never put before it. In his petition to this Court for writ of certiorari, the Commissioner has for the first time advanced, by his so-called "sharpening" process, the applicability of Article 166-1, as amended, unsupported by Section 166, as being the stepping stone for assertion of tax liability under Section 22(a).

Certainly, in the light of the circumstances within and without the record, no one could say that the Respondent, at any time when this case was pending before the Board, was advised "with fair certainty" that there existed a claim of tax liability against him based upon an alleged applicability of Section 22(a). This Court has said explicitly in *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200 at page 206:

> "Always a taxpayer is entitled to know with fair certainty the basis of the claim against him."

The only basis of "the claim against him" of which the Respondent was advised "with fair certainty", or which could even have been suggested, was an alleged taxability under Section 166. If he was successful in meeting that claim, that was all that could reasonably be expected of him. After all, it lay entirely within the Commissioner's discretion and power to fix any issue he might wish, and he specifically fixed as the issue

in this case taxability under Section 166. Certainly he could have asserted before the Board in the instant case in 1939 the same broad issue he had raised in the *Clifford* case, decided by the Board in his favor in 1938 (Memo. opinion, B. T. A. Docket No. 89054). The Commissioner has no just cause of complaint now in not being permitted to introduce on appeal this totally different and much broader issue. Viewed in the light most favorable to the Commissioner, what he now claims (which he did not claim in the court below) is that he argued in his brief before the Board a theory which could support a Section 22(a) issue, although he does not claim that Section 22(a) was directly put in issue before the Board. Can it be said that the taxpayer was advised "with fair certainty" that such issue was in the case when it was pending before the Board? If the answer should be in the affirmative, it will mean that hereafter no matter how specific an issue is fixed by the Commissioner, the taxpayer for his own protection will have to appeal to the Board and factually present evidence, not only on that issue but on every other issue that later could conceivably be raised under any of the provisions of the entire Revenue Code. No end of disorder would result from such a situation.

POINT II.

Article 166-1 as Amended in 1936 Could Not be the Basis for Assertion of Tax Liability in This Case Under Section 22(a).

While in the preceding Point I we have shown that the Article 166-1, as amended, was never used or even sought to be used by the Commissioner as the basis for asserting tax liability against the Respondent either by itself, or in conjunction with Section 22(a), until this case reached this Court, such Article from the legal

standpoint alone could not be made the basis for establishing the tax liability in this case. Taxability is established by statute not by regulations. See Brown, *Regulations, Reenactment and the Revenue Acts,* 54 Harv. L. Rev. 377, 397, for need of a pronouncement by this Court.

To begin with, a taxpayer must be able to place reliance upon what is said in the regulations promulgated by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury. According to what a taxpayer is told in the pertinent Regulations 86 (and similarly in other regulations over a period of years) he has the right to rely, on the fact that each article or series of articles interprets only that section of statute it follows. That each article of the regulations stems from, and is intended to interpret, a particular section of the Revenue Act appears from Article I of Treasury Regulations 86, interpreting sections of the Revenue Act of 1934. This Article states:

> "Scope of regulations.—These regulations deal with the tax upon net income imposed by Title I of the Revenue Act of 1934 . . ."
>
> "The articles bearing a given key number are the regulations promulgated with respect to the corresponding section, subsection, or paragraph of the Act; and the section, subsection, or paragraph of the Act shall be considered as a part of the respective articles to which it corresponds."

On page III of the Introductory Statement to these Regulations, it is stated:

> "The plan has been adopted by using the numbers of the Act as key numbers, followed by a dash (—), with the number of the article placed after the dash. By this means anyone who desires to learn how a given section or subsection of the Act

has been interpreted by the Bureau can readily and quickly find that interpretation by using the key number. Thus, if one desires to learn what interpretation has been placed on section 26 of the Act, he should turn to article 26-1 of the regulations."

Article 166-1 was not promulgated under Section 22(a); it was promulgated under Section 166, and, as appears from the foregoing quotation from the regulations themselves, it was applicable only to Section 166. That, too, was the Commissioner's view when the case was before the Board, for he asserted in the ninety day letter, by brief and in his assignments of error that the Respondent was taxable under Section 166. It should be noted that nowhere in Article 166-1, as amended, is there any cross reference to Section 22(a) or the regulations thereunder although there are cross references to other sections of the Revenue Act. Similarly, the regulations under Section 22(a) make no cross references to Section 166 or Article 166-1. Yet throughout the regulations there are innumerable cross references, which indicates clearly that there never was intended to be any connection between Section 22(a) and Article 166-1, as amended, and that the present claim to that effect is merely an afterthought.

Furthermore, Article 166-1, as amended in 1936 could not be the basis for asserting tax liability for the year 1934. *Helvering* v. *Wood,* 309 U. S. 344; *Helvering* v. *Clifford,* 309 U. S 331. Thus this Court in these recent cases has twice indicated on the merits that Article 166-1, as amended, can not be a stepping stone to taxation of 1934 income under Section 22(a). The *Wood* case is similar to the instant case in all important respects. In both cases the issue tried in the Board of Tax Appeals was on the basis of Section 166; while on appeal the Commissioner asserted taxability on the

basis of Section 22(a). It appears from the opinion in the *Wood* case that the Commissioner also advanced in this Court, as in the instant case, Article 166-1, as amended, as a ground for his shifting to the new issue. This Court merely noted that Article 166-1, as amended, could not have been relied upon to tax 1934 income under Section 22(a). A similar notation appears in the opinion of this Court in the *Clifford* case. In the latter case Section 22(a) was found to be applicable to the issues raised in the Board, but it was noted that Article 166-1, as amended, could not be considered an appropriate regulation on which to assert taxability for the year 1934 under Section 22(a). It is clear that while Treasury Decision 4629 necessarily amended the regulations then in effect, the amendment is only given effect in Regulations 94 which deal with taxes imposed by the Revenue Act of 1936. For reasons against the retroactive application of amended regulations, see Griswold, *A Summary of the Regulations Problem,* 54 Harv. L. Rev. 398. In the *Clifford* and *Wood* cases, the Court was merely following the precedent laid down by it in *Helvering* v. *Reynolds Tobacco Co.,* 306 U. S. 110, where a change in regulations was involved, and the Court said, at page 116:

> "We hold that the respondent's tax liability for the year 1929 is to be determined in conformity to the regulation then in force."

In that case also an amended regulation was advanced in an effort to include within the scope of Section 22(a) income which was not previously taxable. The Court's opinion did not find it necessary to distinguish its earlier decision in *Morrissey* v. *Commissioner,* 296 U. S. 344, in which this Court merely applied an amended regulation, which followed a previous decision of the

Court, redefining the category into which the taxpayer fell.

If Article 166-1, as amended, is to be given the broad interpretation sought by the Commissioner, it is plainly invalid as exceeding the scope of Secton 166 which it was promulgated to interpret. His brief indicates that irrespective of the scope of Section 166, Article 166-1, as amended, should be treated as a license to him to subject all short term trusts to the general provisions of Section 22(a), even though Congress has never seen fit to do so itself. *Helvering* v. *Wood,* 309 U. S. 344, 348.

POINT III.

The Action of the Circuit Court of Appeals in Refusing to Consider the Applicability of Section 22(a) was Proper and in Keeping With the General Law on the Subject.

The disposition of this case by the Circuit Court of Appeals was in accordance with the only position it could have taken consistent with the principles of appellate procedure approved in many rulings by this Court. The Commissioner had asked the Court to determine an issue which as shown above was a completely new one and one on which the Respondent might or might not have been found taxable before the Board if he had tried the case on that basis. The Circuit Court of Appeals held that it could not consider this new issue. In so doing, that court followed the principle laid down by this Court in many cases.

A case similar to the instant case in its proceedings below is *Burnet* v. *Commonwealth Improvement Co.,* 287 U. S. 415. In that case the taxpayer had raised two points before this Court, although the Board had expressed no opinion on one point which had not been raised. The Circuit Court of Appeals had likewise not

considered it. This Court ruled only on the litigated point, saying (287 U. S. 418):

> "We do not undertake to determine what was not considered below."

Respondent believes that ruling should be applied to the instant case for the same reasons that the Court applied it in the case of *Helvering* v. *Wood,* 309 U. S. 344. Since Section 22(a) was not considered below in either case, although raised for the first time in the instant case in the Circuit Court of Appeals, it would seem to make little difference whether that issue had been expressly waived as in the *Wood* case in the Circuit Court of Appeals or implicitly waived as in the instant case in the Board and also to begin with in the Circuit Court of Appeals (*supra,* p. 11). In both cases the taxpayer had every reason to think there was no such issue at all in the earlier stages of litigation.

This principle, which this Court has applied to its own considerations, it has also applied to those of the Circuit Courts of Appeals. Thus, in *General Utilities & Operating Co.* v. *Helvering,* 296 U. S. 200, this Court reversed a Circuit Court of Appeals where that court had held in favor of the Commissioner upon a ground not raised before the Board of Tax Appeals. At page 206 this Court stated:

> "The second ground of objection, although sustained by the court, was not presented to or ruled upon by the Board. The petition for review relied wholly upon the first point; and, in the circumstances, we think the court should have considered no other."

In the instant case there was no issue left for consideration since the Commissioner expressly abandoned the one issue upon which he had wholly relied in his pe-

tition for review. Therefore, the Circuit Court of Appeals could only rely upon the above ruling and affirm the Board's decision.

Moreover, this Court rebuked the Circuit Court of Appeals in *Helvering* v. *Salvage,* 297 U. S. 106, where that Court had considered a claim of estoppel which had neither been presented to the Board of Tax Appeals nor considered by it. In that case it was stated, at page 109:

> "The defense of estoppel was not before the Board. Under what we regard as the correct practice, *General Utilities & Operating Co.* v. *Helvering,* 296 U. S. 200 * * *, the court should have passed the point."

On the other hand, in *Helvering* v. *Pfeiffer,* 302 U. S. 247, this Court approved the action of the Circuit Court of Appeals, which had said: "The contention that we have authority to sustain the deficiency *pro tanto* even though the issue was not raised before the Board nor decided by it nor assigned as error in the petition to this Court for a review of the Board's decision is untenable." (88 F. (2d) 3, 5.) This Court said (302 U. S. at 250):

> "We are not at liberty to entertain that contention."

It will be noted that in all of the cases heretofore cited, this Court did not remand the case to the Board of Tax Appeals for trial of the new issue. It would be manifestly unfair to a taxpayer to require him, after he had defended his position before the Board and before two courts of review, to begin all over and to defend himself again by all necessary processes through trial and review against further charges made by the Commissioner for the first time on appeal.

The principle of appellate procedure which this Court has laid down to govern appeals before it and before the Circuit Court of Appeals is particularly applicable to tax cases. In *Blair* v. *Oesterlein Mach. Co.*, 275 U. S. 220, 225, this Court pointed out:

> "We think the question suggested is not properly before us. It was not specifically raised on the record before the Board or either court below and, so far as appears, was not considered by any of them. We were asked to grant certiorari only to pass upon the question whether the Commissioner's determinations under §§ 327 and 328 may be appealed to the Board of Tax Appeals. This Court sits as a court of review. It is only in exceptional cases, and then only in cases from the federal courts, that questions not pressed or passed upon below are considered here. *Duignan* v. *United States*, 274 U. S. 195. There are specially cogent reasons why this rule should be adhered to when the question involves a practice of one of the great departments of the government."

In a later case this Court noted some of the reasons why this principle should prevail in tax cases. In *Helvering* v. *Tex-Penn Oil Co.*, 300 U. S. 481, it is said at page 498:

> "The taxpayers were entitled to know the basis of law and fact on which the Commissioner sought to sustain the deficiencies. His failure earlier to present the question leaves this court without the assistance of decision below."

One of the reasons advanced there, the lack of assistance by an opinion of the lower court, was also pointed out in *Helvering* v. *Wood*, 309 U. S. 344, 349. Another compelling reason why this principle should prevail has been succinctly stated by the court below in re-

fusing to consider the new issue in the instant case (R. 29):

> "Obviously many facts which would be totally irrelevant to the issue which was presented to the Board might be pertinent and even determinative of the issue now sought to be raised for the first time in this court. The possibility of prejudice to the taxpayer appears to us to be self evident."

Had the Respondent been advised with fair certainty before the Board of the basis of the claim now asserted against him, he could have adduced additional, relevant evidence and otherwise have prepared the case for trial, so that the Commissioner's present position would not operate to his prejudice. Respondent believes that the principle of appellate procedure, the reasons for the principle, and the reasons for its application to the instant case are too clear to admit of argument. As applied where a new issue is urged for reversal, this Court said in the *Wood* case, after refusing its consideration (309 U. S. at 349):

> "It is not apparent why a less strict rule is necessary in order adequately to protect the revenue."

As to the introduction of the new issue of Section 22(a), the instant case, when it was before the Circuit Court of Appeals, was generally in the same relative position as the *Wood* case when it came before this Court. In each instance, for the first time, the applicability of Section 22(a) was urged. In the *Wood* case, this Court refused to pass upon the new issue raised before it for the first time. Nor did it remand that case. The Circuit Court of Appeals in the instant case did likewise, although it should be noted that Section 22(a) was not originally urged in the assignments

of error before the Circuit Court of Appeals, whereas Section 22(a) was urged in the petition for writ of certiorari in the *Wood* case. The Commissioner in his brief emphasizes the fact that this Court in the *Wood* case specifically referred to the waiver of the issue of Section 22(a) before the lower court. However, in the light of what has been said by this Court in the past, we do not assume that in the *Wood* case the main harm was done by waiver before the lower court. The harm was done initially when the initial tribunal, which is the trier of the facts and of the law as they are presented to it, had not had the opportunity to pass upon the subsequently raised issue. That same disadvantageous situation obtains whether the issue is raised for the first time in the Circuit Court of Appeals or for the first time in this Court. The Circuit Court of Appeals has no greater means of trying the facts upon the new issue than does this Court.

Obviously there are exceptions to the principle or rule referred to above which may be allowed when they do not operate to the prejudice of the parties or the appellate court. Thus, a court may consider a new argument or reason, advanced usually by the appellee, *to support* the determination reached by a lower court or board. Cf. *Helvering* v. *Gowran,* 302 U. S. 238; *Helvering* v. *Rankin,* 295 U. S. 123. That practice has been indulged by this Court to support the trial tribunal for a reason which had not been advanced in the appellate court below. Cf. *Helvering* v. *Leonard,* 310 U. S. 80, where taxability was asserted before the Board and the appellate court under the rule of *Douglas* v. *Willcuts,* 296 U. S. 1, and this Court found the taxpayer liable under that rule, reinstating the decision of the Board, for a reason not advanced in the Circuit Court of Appeals. But even in that case, the

Court had all pertinent facts before it; the respondent was not prejudiced and did not object to the raising of the new reason. That could not be the situation where, as here, a whole new issue involving much broader questions of law and fact was sought to be raised for the first time in the appellate court for the purpose of reversing the trial tribunal.

We think it unnecessary to comment at length on the many cases cited by the Commissioner in his brief as having to do with the question of raising new issues on appeal. Beside the point are those cases which hold that to support a decision of the initial tribunal the appellee may raise questions not raised below[1]. That is not the case here. Also beside the point are those exceptional cases in which to prevent injustice, courts have permitted the appellant to raise some new point of law where all the salient facts are before the appellate court[2]. In such cases the new point involved purely a question of law. That is not the case here and there are here no exceptional circumstances, a fact which was recognized in the *Wood* case.

Another group of cases which are not pertinent to the instant situation are those in which the appellate court, upon review of the issue decided below, found the record incomplete and therefore remanded the case for further findings necessary to a final determination[3].

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[1] *Helvering* v. *Gowran*, 302 U. S. 238.
Helvering v. *Rankin*, 295 U. S. 123.
Langnes v. *Green*, 282 U. S. 531, 539.

[2] *Legg's Estate* v. *Commissioner*, 114 F. (2d) 760 (C. C. A. 4th).
United States v. *Spalding*, 115 F. (2d) 54 (C. C. A. 5th).
Seufert Bros. v. *Lucas*, 44 F. (2d) 5-8 (C. C. A. 9th).

[3] *Edwards* v. *Holland Banking Co.*, 75 F. (2d) 713 (C. C. A. 8th).
Hamilton Gas Co. v. *Watters*, 75 F. (2d) 170 (C. C. A. 4th).
Eau Claire Book & Stationery Co. v. *Commissioners*, 65 F. (2d) 185 (C. C. A. 7th).
Underwood v. *Commissioner*, 56 F. (2d) 67 (C. C. A. 4th).

Likewise beside the point are those cases in which the issue was raised and passed on by the trial tribunal and then decided in the appellate court on a correct application of the law[1]. Into this category fall also sundry other cases where the law applicable to the issue was changed between trial and appeal. Such cases have no bearing here where the issue itself was not raised until after appeal had been taken.

We fail to see how under any circumstances the Circuit Court of Appeals can consider the new issue of the applicability of Section 22(a), involving as it does new and different questions. In the words of this Court, the issue under Section 22(a) "is whether the grantor after the trust has been established may still be treated, under this statutory scheme, as the owner of the corpus." *Helvering* v. *Clifford*, 309 U. S. 331, 334. The Court then said, at page 335:

> "The answer to that question must depend on an analysis of the terms of the trust and all the circumstances attendant on its creation and operation."

At page 338, this Court found that to determine such an issue it was necessary:

> "to leave to the triers of fact, the initial determination of whether or not, on the facts of each case, the grantor remains the owner for purposes of § 22(a)."

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[1] *Helvering* v. *Clifford*, 309 U. S. 331.
Sibbach v. *Wilson Co.* (U. S., December 13, 1940).
Commissioner v. *Berolzheimer*, (C. C. A. 2nd, December 23, 1940) (unofficially reported C. C. H. par. 9156), see 40 B. T. A. 645, 646, 648.
White v. *Higgins*, (C. C. A. 1, December 12, 1940) (unofficially reported C. C. H. par. 9136).

Contrary to Commissioner's present implication, there can be no presumption that Section 22(a) will make all trust income taxable, even if the trust be of short duration. Congress itself has not seen fit to do so. From what has been said above, it is obvious that a new and broader issue asserted by the Commissioner involves questions of fact as well as of law.

In the instant case, it is apparent that the facts which were stipulated were limited to those dealing with Section 166 and bearing on the question of revocability of the trust and not with regard to a far broader issue that would have been raised by Section 22(a). How, therefore, could the Circuit Court of Appeals then, or how can it now, with any propriety find Respondent taxable under Section 22(a)? As this Court said in *Helvering* v. *Wood*, 309 U. S. 344, 349:

> "The issues under § 166 and § 22(a) are not coterminous. Though both deal with concepts of ownership, the range of inquiry under the latter is broad, under the former confined."

Again, at page 347, it is said:

> "The problem of interpretation under § 166 is therefore quite different from that under § 22(a)."

In the light of what this Court has said, both with regard to the principle of appellate procedure and with regard to the factual requirements for determination of a broad issue based upon Section 22(a), this Court, we submit, should affirm the decision of the Circuit Court of Appeals, which was correct in its disposition of the case, for, under the limited question for review by this Court, that is, whether or not the Circuit Court of Appeals was correct in its action, there is nothing

which would enable the lower court to determine the new and broader issue based on Section 22(a).

CONCLUSION.

It is submitted that the decision of the court below should be affirmed.

Respectfully,

RICHARD H. WILMER,
DOUGLAS L. HATCH,
Attorneys for Respondent.

APPENDIX.

Excerpt from Table of Contents of Respondent's (Taxpayer's) Brief before the Board of Tax Appeals.

Argument

Preliminary Statement

Point I—A and B

No "Power to Revest in the" Petitioner "Title to any Part of the Corpus of the Trust" was Vested in the Grantor in Conjunction with a Person not Having a Substantial Adverse Interest in the Disposition of the Corpus or the Income Therefrom, for

A. The grantor's reversionary interest after the termination of the trust is not a "power to revest" within the meaning of Section 166 of the Revenue Act of 1934, or

B. The events of revesting of the corpus, namely, the death of the grantor or the death of the beneficiary, are not events of "power to revest" in the grantor.

Point I—C

No "Power to Revest in the" Petitioner "Title to any Part of the Corpus of the Trust" was Vested in the Grantor in Conjunction with a Person not Having a Substantial Adverse Interest in the Disposition of the Corpus or the Income Therefrom, for

C. The only "power to revest" in the grantor was with the consent of a person having a substantial adverse interest, namely, the beneficiary, and, therefore, expressly without the provisions of Section 166 of the Revenue Act of 1934.

Summary of Point I

Point II

The Attempt of the Respondent to Tax Petitioner on the Income Arising under the Trust is an Unconstitutional Exercise of the Taxing Power.

Point III

The Determination of the Commissioner should be set Aside.

Page 2 of Commissioner's Brief before the Board.

Question Presented.

Is the income realized by the trust created by the petitioner on December 29, 1930 taxable to the petitioner as grantor under the provisions of section 166 of the Revenue Act of 1934?

Motion of Commissioner in Circuit Court of Appeals for extension of time to complete and transmit the certified transcript of record on review.

Motion.

NOW COMES the Commissioner of Internal Revenue, petitioner on review in the above-entitled cause, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and

MOVES that the time within which to complete and transmit the certified transcript of record on review in the above-entitled cause to the United States Circuit Court of Appeals for the Third Circuit be extended from December 12, 1939 to and including May 1, 1940, and in support of this motion respectfully shows that:

1. On October 13, 1939 the Commissioner filed with the Board a petition seeking review of the Board's

decision in this cause by the United States Circuit Court of Appeals for the Third Circuit.

2. The issue involved in this case is similar to that presented in the case of *Commissioner* v. *Meredith Wood,* B. T. A. Docket No. 88426 (37 B. T. A. 1065), affirmed *per curiam* by the United States Circuit Court of Appeals for the Second Circuit May 29, 1939.

3. Petition for writ of certiorari in the case of *Meredith Wood, supra,* was filed on September 13, 1939 and granted by the Supreme Court November 6, 1939.

4. It is to the advantage of both parties to withhold the preparation, transmission, and delivery of the printed record *sur* petition for review in this case until the decision of the Supreme Court becomes final in the *Wood* case, which is not expected before May 1, 1940.

(signed) J. P. WENCHEL,
RLW
J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

JOHN W. SMITH,
Special Attorney,
Bureau of Internal Revenue.

No Objection:

(signed) DOUGLAS L. HATCH,
Attorney for Respondent on Review.

JWS:cm 11-25-39

SUPREME COURT OF THE UNITED STATES.

No. 516.—October Term, 1940.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* O. G. Richter. } On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[March 17, 1941.]

Mr. Justice Black delivered the opinion of the Court.

Because the decision below, 114 F. (2d) 452, was in conflict with that of the Circuit Court of Appeals for the Eighth Circuit in *Helvering* v. *Hormel,* 111 F. (2d) 1, affirmed this day, we granted certiorari "limited to the first question presented by the petition for the writ." 311 U. S. —. The petition stated that question as follows:

"The taxpayer transferred securities to a third party in trust to pay the income to his wife. At the end of five years, or earlier if the beneficiary consented, the securities were to be transferred back to the taxpayer. The Board of Tax Appeals held that the grantor was not taxable with respect to the income from the trust. Two questions are presented:

"1. Whether, by invoking the general gross income provisions of Section 22, the Commissioner had so changed the theory of the Government's case on appeal as to preclude the Circuit Court of Appeals from considering the issue.

"2. Whether, on the merits, the trust income was taxable as income of the grantor under Section 22."

In view of the limited grant of certiorari, the second question is not before us. On the first question, the Circuit Court of Appeals held that it could not consider the applicability of section 22(a), that being an "issue now for the first time presented by the Commissioner." The decision of the Board of Tax Appeals, which the Circuit Court of Appeals affirmed, was handed down prior to our decision in *Helvering* v. *Clifford,* 309 U. S. 331. Respondent urges that had he been advised with fair certainty that the government relied upon section 22(a), he could have introduced additional evidence directed to that issue. For reasons set out in our decision

in *Hormel* v. *Helvering*, we are of opinion that the Circuit Court of Appeals was in error in its conclusion, but we are also of opinion that respondent is entitled to introduce additional evidence if he so desires. The judgment is accordingly reversed, with directions to the court below to remand to the Board of Tax Appeals for rehearing in the light of the *Clifford* case.

Reversed.

A true copy.

Test:

Clerk, Supreme Court, U. S.